

4 FAM 730

INVENTORY AND PROPERTY, PLANT, AND EQUIPMENT

(CT:FIN-437; 01-08-2015)
(Office of Origin: CGFS/FPRA/FP)

4 FAM 731 PURPOSE AND AUTHORITY

4 FAM 731.1 Purpose

(CT:FIN-394; 08-15-2008)

This subchapter provides the financial management policies for accounting of and reporting on Department of State inventory and property. It covers the basic requirements for designating inventory, operating materials, and for personal, intangible, and real property, as well as the costs that must be accumulated and reported for each designation.

4 FAM 731.2 Authority

(CT:FIN-414; 05-05-2011)

- a. 31 U.S.C. 3512(b) provides that each executive agency shall establish and maintain systems of accounting and internal controls that provide effective control over, and accountability for, assets for which the agency is responsible.
- b. Other legislation that impacts the provisions in this subchapter include:
 - (1) Chief Financial Officers Act (CFO), 31 U.S.C. 901 - 903;
 - (2) Federal Manager's Financial Integrity Act (FMFIA), Public Law 97-255 (1982);
 - (3) Federal Financial Management Improvement Act (FFMIA), Public Law 104-208, sec. 801 et seq. (1996); and
 - (4) The Information Technology Management Reform Act of 1996 (Clinger-Cohen Act), sec. 5126, 40 U.S.C. 11316.
- c. Other relevant regulations and guidance include:
 - (1) OMB Circular A-123, Management Responsibility for Internal Controls;
 - (2) OMB Circular A-126, Improving the Management and Use of Government Aircraft;

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- (3) OMB Circular A-134, Financial Accounting Principles and Standards; and
 - (4) Federal Management Regulations, 41 CFR 102-33 (Management of Government Aircraft).
- d. Statement of Federal Financial Accounting Standards (SFFAS). OMB Circular A-134 provides that "SFFASs shall be considered generally accepted accounting principles (GAAP) for Federal agencies. Agencies shall apply the SFFASs in preparing financial statements in accordance with the requirements of the Chief Financial Officers Act of 1990."

4 FAM 732 INVENTORY AND OPERATING MATERIALS

(CT:FIN-433; 09-13-2013)

- a. Inventory is tangible personal property that is:
 - (1) Held for sale;
 - (2) In the process of production for sale; or
 - (3) To be consumed in the production of goods for sale or in the provision of services.
- b. Operating materials and supplies consist of tangible personal property to be consumed in normal operations. Specific items excluded from operating materials are:
 - (1) Goods that have been acquired for use in the construction of real property or in assembling equipment to be used by the entity;
 - (2) Stockpiled materials;
 - (3) Goods held under price stabilization programs;
 - (4) Foreclosed property;
 - (5) Seized and forfeited property; and
 - (6) Inventory.
- c. Additional information is found in SFFAS No. 3.

4 FAM 732.1 Accounting for Inventory

(CT:FIN-394; 08-15-2008)

The Department has inventory items for sale at domestic facilities and facilities abroad under the Working Capital Fund, as well as publications held for sale at the regional printing offices abroad. The inventory values, namely furniture, publications, and raw materials used in the production of publications, are recorded in the Department's general ledger. The inventories are valued in

accordance with accepted valuation methods (e.g., weighted moving average for the Washington Logistics Center and stock account and the cost of production for publications held for sale) and are adjusted for the results of periodic physical inventories.

4 FAM 732.2 Accounting for Operating Materials

(CT:FIN-433; 09-13-2013)

- a. SFFAS No. 3 permits individual agencies to use the purchase method (instead of the consumption method) of accounting for the recognition of expenses of operating materials and supplies if:
 - (1) The materials and supplies are not significant amounts;
 - (2) The materials and supplies are not in the hands of the end user; or
 - (3) It is not cost beneficial to apply the consumption method.
- b. In accordance with these principles, the Department has determined that the purchase method is the appropriate method for treating all operating materials. All operating materials and supplies should be expensed when purchased.

4 FAM 733 PROPERTY, PLANT, AND EQUIPMENT (PP&E) GENERAL PROVISIONS

(CT:FIN-433; 09-13-2013)

- a. Under the Federal Financial Management Improvement Act of 1996, the Department is required to implement financial management systems that comply with Federal accounting standards, which include the Statements of Federal Financial Accounting Standards (SFFAS) governing property, plant, and equipment. The accounting standards for property are provided in SFFAS Nos. 6, 8, 10, 11, 14, 16, and 23.
- b. Sections 4 FAM 733.1 through 4 FAM 736.3 contain the Department of State's accounting policy pertaining to the accounting for personal property. Policies and procedures for personal property management in accordance with applicable General Services Administration and other regulations may be found in 14 FAH-1, Department-Wide Personal Property Management Handbook.
- c. Property, plant, and equipment are assets that are acquired by procurement, transfer, capital lease, donation, or other method that transfers ownership and have the following characteristics:
 - (1) A useful life of 2 or more years;
 - (2) Not intended for sale; and
 - (3) Intended to be used to conduct business.

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- d. Assets that are classified as personal property must be accounted for in accordance with the designations identified in 4 FAM 733.1.

4 FAM 733.1 Property, Plant, and Equipment (PP&E) Designations and Classifications for Personal Property

(CT:FIN-433; 09-13-2013)

SFFAS No. 6, as amended by subsequent standards, requires personal property to be designated as either:

- (1) General; or
- (2) Heritage.

4 FAM 733.1-1 General Property, Plant, and Equipment (PP&E)

(CT:FIN-414; 05-05-2011)

- a. General PP&E consists of items that are used:
- (1) To produce goods or services or to support the mission of the entity and can be used for alternative purposes (e.g., by other Federal programs, State and local governments, or nongovernmental entities);
 - (2) In business-type activities; or
 - (3) By U.S. Government entities in activities whose costs can be compared to other entities.
- b. Most personal property in use in the Department is general PP&E. Unless the personal property meets the specific definition for heritage assets, the property is designated as general purpose. It is recorded at acquisition cost in the appropriate general ledger account if it equals or exceeds the capitalization threshold for the asset type. The cost recorded will be consistent with the cost requirements for property accountability (see 14 FAH-1 H-415.2) and the capitalized cost requirements in 4 FAM 734 and 4 FAM 735. Indirect costs will be added to the capitalized cost basis when 4 FAM 734.1 is applicable. Examples of general PP&E include vehicles, communications equipment, reproduction equipment, medical equipment, information technology (IT) hardware, aircraft, and software.
- c. Except for software, software-in-development, and property located in high-risk areas, personal property is depreciated (straight-line method) in accordance with the estimated useful life of the property. Software is amortized in accordance with the capitalization policy in 4 FAM 735.1; the capitalization thresholds identified in 4 FAM 734.2, subparagraph a(4); and the amortization policy in 4 FAM 734.3, subparagraph (3). The high-risk property depreciation convention is identified in 4 FAM 736.3.

4 FAM 733.1-2 Special Rules for Some Categories of General Property, Plant, and Equipment (PP&E)

(CT:FIN-433; 09-13-2013)

- a. Internal-use software is generally classified as general property under SFFAS No. 6. However, internal-use software has special accounting requirements that must be followed under SFFAS No. 10, Internal Use Software, for software designed for internal use and acquired after October 1, 2001. All Department software is classified as intangible general property, even if it is used to support property with a different designation (e.g., heritage). The accounting treatment for internal-use software is identified in 4 FAM 735.
- b. Software developed to perform functions for internal business needs is recorded as a separate intangible asset in the Department's general ledger. However, when the software in personal property is not separately identified by the manufacturer at the time of procurement, it does not have to be separately capitalized in the Department's general ledger. If the personal property requires a future software upgrade that meets the criteria in 4 FAM 735, the software upgrade cost should be considered an integral part of the general PP&E and must be identified and recorded. The aggregate cost of upgraded software should be used to determine whether to capitalize or expense the cost.
- c. U.S. Government-owned property in the hands of Department contractors is general PP&E and must be identified and reported on Department financial statements in a manner consistent with the requirements of this subchapter (see 4 FAM 736). U.S. Government-leased property provided to contractors must not be identified or recorded in the general ledger as U.S. Government-owned. Special property accounting rules are applied to contractor-held assets maintained in a hostile program environment (see 4 FAM 736.3).
- d. Aircraft assets managed by the Bureau of International Narcotics and Law Enforcement Affairs (INL) are general PP&E and are subject to provisions in SFFAS No. 6, as well as OMB Circular A-126 and the Federal Management Regulations, 41 CFR 102-33, Management of Government Aircraft. There are special rules related to accounting for aircraft assets contained in 4 FAM 736.2-1. Fixed-wing, rotary aircraft, and component spare property for aviation operations must be associated with a separate asset class (see 4 FAM 733.1-3, paragraph b).

4 FAM 733.1-3 General Personal Property, Plant, and Equipment (PP&E) Classifications

(CT:FIN-394; 08-15-2008)

- a. For general property, separate general ledger accounts must be used for significant classifications of personal property. Common classifications must be used for both accounting and property management purposes. The

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classification also identifies types of property for which value must be regularly reported to the Congress or other executive agencies.

- b. The financial management system classifies personal property according to the following categories:
 - (1) Vehicles (see paragraph c of this section);
 - (2) Communications equipment;
 - (3) Information technology (formerly called automated data processing) equipment;
 - (4) Reproduction equipment;
 - (5) Security equipment;
 - (6) Software;
 - (7) Software-in-development;
 - (8) Medical equipment;
 - (9) Aircraft property; and
 - (10) Other depreciable personal property.
- c. The classification of property as vehicles must be in accordance with Office of Logistics Management (A/LM) guidance. Property acquisitions for all human-powered or nonmotorized transportation property, such as bicycles, tricycles, scooters, wagons, trailers, etc., are not to be classified as vehicles. These property items should be classified as "other" personal property and subject to the applicable personal property capitalization threshold, when warranted. Salvage values for motor vehicles will be 10 percent, except for vehicles subject to Bureau of Diplomatic Security (DS) disposal guidance (see 12 FAM 388 (armored vehicles)) or contractor-held vehicles in high-risk areas, which will have zero salvage value in accordance with 4 FAM 736.3. Commercially leased and General Services Administration (GSA) fleet-leased vehicles must not be identified as U.S. Government-owned property in the financial management system.

4 FAM 733.2 Heritage Property

(CT:FIN-414; 05-05-2011)

- a. To be characterized as heritage PP&E, an item should have:
 - (1) Historical or natural significance;
 - (2) Cultural, educational, or artistic importance; or
 - (3) Significant architectural characteristics.
- b. The acquisition cost for heritage properties is not capitalized unless the property is a multi-use heritage asset, which is subject to specific requirements

for financial statement presentation as noted in 4 FAM 733.2-2.

4 FAM 733.2-1 Heritage Personal Property Classifications

(CT:FIN-433; 09-13-2013)

- a. Personal property that may be classified as heritage includes rare books for permanent collections; gift fund items (e.g., antique furniture, rare documents, etc.); and art items identified as works of art in the Department's collections. Heritage personal property is not recorded in the financial management system general ledger as an asset, and cost information is disclosed in the financial statements in accordance with 4 FAM 733.2-3. However, property accountability records must be maintained, and the assets should be valued for insurance purposes.
- b. Except as provided in 4 FAM 733.2-2, the acquisition cost of a heritage asset must be recognized as an expense in the period incurred and is not capitalized. Except as provided in 4 FAM 733.2-2, the cost of improving, reconstructing, or renovating a heritage asset must be recognized as an expense in the period incurred and is not capitalized. If a heritage asset is transferred from another Federal entity, the cost must be the book value of the asset recorded on the transferring entity's books and must be recognized as an expense in the period transferred. There is no cost recognized in the general ledger or for financial reporting for heritage assets acquired through donation or devise.
- c. Procedures for recording personal property heritage assets in Department financial management systems may vary by oversight organization and type of asset being managed. Questions regarding recording requirements and specific procedures to follow should be addressed to the Bureau of the Comptroller and Global Financial Services, Financial Policy, Reporting and Analysis Directorate (CGFS/FPRA).

4 FAM 733.2-2 Multi-Use Heritage Asset Costs

(CT:FIN-414; 05-05-2011)

- a. Heritage property may have dual functions—a heritage function and a general U.S. Government operations function. A heritage asset is considered a "multi-use" heritage asset if its predominant use is general U.S. Government operations. A heritage asset having only an incidental use in U.S. Government operations is designated as a heritage asset.
- b. If the heritage asset is a multi-use heritage asset, the accounting procedures for general property apply. The costs of acquisition and/or refurbishment of multi-use heritage assets are expensed or capitalized in accordance with cost thresholds associated with general PP&E. Depreciation of these capitalized costs will be consistent with depreciation conventions for general PP&E and disclosed as part of general PP&E costs.

4 FAM 733.2-3 Disclosure of Heritage Assets

(CT:FIN-433; 09-13-2013)

Heritage assets are disclosed in the required supplementary information (RSI) section of the financial statements. The heritage assets disclosed include personal property, collections, rare books and manuscripts, and any other items in the Department's historical collections. Disclosure is presented in aggregate totals and must include a description, count of acquisitions and withdrawals, condition, number of items, and status of deferred maintenance. In addition, Statement of Federal Financial Accounting Standards (SFFAS) No. 29 requires the disclosure of entity stewardship policies and how heritage property relates to the mission of the Department. There is no depreciation expense associated with these assets unless they are multi-use heritage assets.

4 FAM 733.3 Property Records and Systems

(CT:FIN-394; 08-15-2008)

- a. The financial management system must accurately reflect the acquisition cost of capitalized personal property in various categories and the accumulated depreciation/amortization (see 4 FAM 733.1-1 and 4 FAM 734.3). Procurement, property record maintenance, and related accounting operations must be integrated so that entries to the subsidiary property records and control accounts are accomplished essentially from the same document, thus creating a single set of records for property.
- b. The Department uses a fixed asset module in the official financial management system to record property costs in the general ledger accounts. The information in this module is supported by property management systems administered by other organizations, such as the Integrated Logistics Management System. These property management systems must therefore contain common data elements and standardized formats compatible with the financial management system.

4 FAM 733.4 Reconciliation of Financial Accounting Records to Property Accountability Records

(CT:FIN-414; 05-05-2011)

- a. The responsible property officers in bureaus and posts must conduct physical counts of PP&E personal property at regular intervals, as specified in regulations in 14 FAM 410 and 14 FAM 420. All property holding, including the capitalized property from this physical inventory procedure, must be reported to the Office of Logistics Management (A/LM). The schedules and procedures for taking such counts are established in 14 FAH-1 H-600.
- b. Inventory procedures and accounting record adjustments must be applied on a

consistent basis from one fiscal year to another. All U.S. Government-owned capitalized personal property, including Bureau of International Narcotics and Law Enforcement Affairs (INL) aviation assets and U.S. Government-owned property held by contractors, will be reconciled to the records used for tracking such property. U.S. Government-leased property is not part of this reconciliation, since leased property is not recorded in the financial management system general ledgers. Adjustments will be made in the official financial management system based on the reconciled information recorded in the property management systems.

4 FAM 733.5 Accounting Classification and Conveyance Requirements

(CT:FIN-433; 09-13-2013)

- a. **Disposition of property.** Property accounts must be adjusted for both acquisition cost and depreciation values of retirements, losses, or other means of property disposal, including property destroyed or demolished. Removal costs and amounts realized must be considered in determining the loss or gain on the disposition of property. Gains and losses on disposal of assets are recognized separately in the accounts.
- b. **Trade-ins.** The cost recorded for property acquired as a result of trade-ins with a private vendor or another Federal entity must be the lesser of:
 - (1) The cash paid or payable, plus the amount allowed by the seller on the trade-in property; or
 - (2) The purchase price of the property acquired if there had been no trade-in.Gains or losses realized on trade-ins are recorded in separate accounts. The amount of gain or loss is the difference between the value of the property received and the value of any materials and services exchanged.
- c. **Reimbursable transfers.** Property transferred to the Department's custody on a reimbursable basis from other Federal agencies must be accounted for on the basis of the transfer price as determined by agreement or application of appropriate statutory requirements or regulations, but at not less than its estimated fair value.
- d. **Transfers from other Federal entities.** The cost of the property transferred without reimbursement from other Federal agencies must be the cost recorded by the transferring entity less the accumulated depreciation or amortization. If these amounts cannot be determined, the cost of the property must be its fair value at the time transferred.
- e. **Donations, devise, judicial process.** The cost of general personal property acquired through donations, devise (bequest), or judicial process (excluding forfeiture) must be the estimated fair value of the property at the time acquired by the Department.

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- f. **Forfeiture.** The cost of property acquired through forfeiture must be determined in accordance with the specific property accounting treatment described in SFFAS No. 3.
- g. **Exchange.** The cost of property acquired through exchange with a non-Federal entity must be the fair value of the property surrendered at the time of the exchange. If the fair value of the property acquired is more readily determinable than that of the property surrendered, the cost must be the fair value of the property acquired. If neither fair value is determinable, the cost must be the cost of the property surrendered (less any accumulated depreciation or amortization). Any difference between the net book value of the property surrendered and the cost of the property acquired must be recognized as a gain or loss. If cash consideration is included in the exchange, the cost of the property acquired must be increased by the amount of the cash paid or decreased by the amount of the cash received.

4 FAM 733.6 Responsibility for Property, Plant, and Equipment (PP&E) Accounting

(CT:FIN-433; 09-13-2013)

- a. Various organizations share responsibilities for accounting for property with the Bureau of the Comptroller and Global Financial Services (CGFS). CGFS maintains the property subsidiary ledgers for financial reporting within the financial management system and is responsible for providing guidance to other bureaus concerning the accounting policies and procedures for property.
- b. The Department organization responsible for the acquisition, improvement, repair, or refurbishment of property must record the property in a Department-approved property management system (e.g., Integrated Logistics Management System (ILMS)). If there is property maintained in systems that do not have automated interfaces with the financial management property subsidiary, the responsible organization must establish a process with CGFS to record the acquisition, disposal, and cost information in the financial management system subsidiary property ledgers. The responsible organization must ensure timely and accurate reporting in its property management system for all property acquisitions, transfers, and disposals.
- c. Responsibilities for tracking software development costs are described in 4 FAM 733.7.
- d. For U.S. Government-owned property held by contractors, the contracting officer representative or designee from the responsible organizations is responsible for tracking and recording the property as described in 4 FAM 736.1. U.S. Government-leased property held by contractors may be tracked for accountability purposes consistent with Office of Logistics Management (A/LM) guidance, but such property is not reflected in the general ledgers of the financial management system. Definitions and supplemental information for

property held by contractors may be found in Federal Acquisition Regulation (FAR) Part 45, Government Property.

4 FAM 733.7 Responsibility for Tracking Software Development Costs

(CT:FIN-433; 09-13-2013)

- a. Program offices responsible for developing or procuring software must follow Bureau of the Comptroller and Global Financial Services (CGFS) requirements to track and capture costs for software investments. CGFS must maintain software in development and finished software subsidiary ledgers to meet reporting requirements under SFFAS No. 10. Therefore, any organization undertaking a software development initiative must establish a project-based process that identifies an initiation and termination/completion of software development investments (see 5 FAM 600 for required project processes).
- b. If software meeting the definitions and conditions identified in 4 FAM 735 is procured as part of a larger initiative, the software cost must be a sufficiently identifiable item within the procurement activity to be accounted for separately as software.
- c. The responsible organization must inform CGFS and the e-Gov Project Management Office of the initiation and completion/termination of each software project, as well as the expected date the software property will be placed in service. This includes the termination of projects prior to completion. Department policy also requires software to be registered in the Information Technology Application Baseline and vetted through the Information Technology Change Control Board (IT CCB) or local Change Control Board (CCB) process before submission to the Bureau of Information Resource Management, Information Assurance Office (IRM/IA) for system authorization review.

4 FAM 734 ACCOUNTING FOR COST OF PERSONAL PROPERTY

(CT:FIN-394; 08-15-2008)

- a. Personal property whose initial acquisition cost exceeds the applicable capitalization threshold (see 4 FAM 733.1-1 and 4 FAM 734.2) must be recorded in the accounts at the cost of bringing the property to a state of usefulness, including transportation to the point of initial use, installation, net of purchase discounts (whether or not taken), and other related costs. When justified for a particular situation, standard or average costing associated with groupings of property is permissible, provided that information as to location and use of each item is maintained.
- b. Capitalized costs for motor vehicles include not only the initial acquisition cost

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but also delivery charges associated with the vehicle, shipping costs to posts abroad, and other preparation costs (e.g., light/heavy armoring, etc.) needed to ready the vehicle for its intended function. Commercially leased or GSA fleet-leased vehicles are not individually capitalized in the financial management system general ledger (see 4 FAM 734.2, paragraph b, for personal property capital leases).

- c. For capitalized general-purpose property transported in bulk via containerized shipments, transportation and related costs must be recorded as follows:
 - (1) When the costs can be readily determined for each item (transportation and related costs), predelivery costs must be distributed and posted to the property records and general ledger accounts;
 - (2) When the costs cannot be readily determined for each item (transportation and related costs), predelivery costs must be charged as current operating expenses.

4 FAM 734.1 Indirect and Overhead Costs for Property

(CT:FIN-433; 09-13-2013)

- a. In addition to capturing the direct costs described in section 4 FAM 735.3, paragraph c, the responsible organization must identify for capitalization purposes the indirect overhead costs associated with software property. Indirect overhead costs for software property must include the following components to the extent that they can be reasonably and consistently allocated to the software property in accordance with subparagraph (1)(b) of this section:
 - (1) Oversight organization salary and benefit costs and/or contractor costs for:
 - (a) Supervisory personnel overseeing staff responsible for multiple software projects;
 - (b) Personnel retained as experts in software design tools;
 - (c) Personnel supporting software development/acquisition; and
 - (d) Office space for direct-hire personnel and/or U.S. Government-furnished space and equipment for contractor personnel;
 - (2) Travel and fixed facility (office space, utilities, supplies, computer hardware, etc.) costs for organization supervisory and other personnel (legal, procurement, financial, administrative, etc.) responsible for supporting software development; and
 - (3) Fees, licenses, and/or other costs for software development activities but are not directly attributed to specific projects.
- b. Indirect costs for software may be calculated as a percentage of direct costs if historical data shows a consistent relationship between direct costs and indirect

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costs. This standard percentage is the preferred method to determine the indirect costs of a project. However, when this method is not appropriate, contact the Bureau of the Comptroller and Global Financial Services, Office of Financial Policy (CGFS/FPRA/FP) for guidance on alternative methods for applying indirect costs under SFFAS No. 4.

- c. Indirect and overhead costs for general personal property do not have to be identified when it is not cost effective to do so and the costs do not have a material impact on the cost basis of the capitalized property.

4 FAM 734.2 Capitalization Criteria for Personal Property

(CT:FIN-437; 01-08-2015)

- a. **Personal property.** Personal property classified as fixed assets must be capitalized or accounted for as follows:
 - (1) Except for property described in subparagraphs a(2), a(3), and a(4) of this section, personal property must be capitalized at the date of acquisition if:
 - (a) It is complete within itself;
 - (b) It does not lose its identity or become a component part of other property when put into use;
 - (c) Its value exceeds \$25,000 on the date of acquisition; and
 - (d) It is of a durable nature with an estimated useful life expectancy to exceed 2 years;
 - (2) Personal property capital leases do not have a threshold. These leases must be recorded at the computed value of the lease terms required by 4 FAM 734.2, paragraph b;
 - (3) All classes of *on-road four-wheeled* motor vehicles *in the post motor vehicle fleets* (e.g., sedans, passenger vehicles, trucks, utility vehicles, vans, etc.) must be fully capitalized regardless of acquisition cost, *including U.S. Government-owned vehicles held by contractors in high-risk locations*. U.S. Government-furnished commercially leased and General Services Administration (GSA) fleet-leased vehicles provided to contractors are not capitalized even though contractors will be required to identify such vehicles when providing a list of all contractor-held property;
 - (4) **Software capitalization thresholds.** Most internal-use software, as defined in 4 FAM 735, must be capitalized if its total cost is equal to or exceeds \$500,000. This means that the procurement options for commercial off-the-shelf (COTS), Government off-the-shelf (GOTS), or mixed-use software, as described in 4 FAM 735.3, paragraph e, must be capitalized if its total cost (e.g., purchase, configure, test, etc.) is equal to or exceeds \$500,000. Individual COTS/GOTS software packages or site

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licenses that equal or exceed \$25,000 in cost and that are acquired as part of a deployment initiative are considered an element of personal property and should be capitalized in accordance with procedures for personal property (see 4 FAM 734.2, subparagraph a(1)). Software that is a component of another piece of personal property is subject to the special rules in 4 FAM 733.1-2.

- b. **Personal property capital leases.** Leases meeting one or more of the following criteria must be classified as capital leases:
- (1) Lease transfers ownership to the U.S. Government at the end of the lease term (i.e., fixed noncancelable term);
 - (2) Lease contains an option to purchase the property at a bargain price;
 - (3) Lease term is equal to 75 percent or more of the estimated economic life of the leased property;
 - (4) Present value at the beginning of the lease of the minimum lease payments is 90 percent or more of the fair value of the leased property.

NOTE: Capital leases must be recorded as an asset and a liability at an amount equal to the net present value at the beginning of the lease of the minimum lease payments during the lease term, excluding costs to be paid by the lessor (taxes, insurance, etc.). However, if the amount so determined exceeds the fair value of the property, the fair value should be recorded.

- c. **Purchases.** Purchases made under lease/purchase contracts that are in fact purchases (the decision to purchase having already been made) are treated for capitalization purposes as installment purchases.

4 FAM 734.3 Depreciation and Amortization Conventions for Personal Property and Software

(CT:FIN-433; 09-13-2013)

The following information provides general guidance on the depreciation and amortization conventions for property, plant, and equipment (PP&E). Depreciation conventions are applied to personal property that has been constructed, purchased, transferred, or exchanged. Amortization conventions are applied to personal property leases and internal-use software:

- (1) **Basic principles.** In accordance with SFFAS No. 6, the accounting system recognizes and records depreciation and amortization on all capitalized general-purpose and mixed-use property. Depreciation begins when the property is placed in service. Depreciation and amortization charges must be recorded down to the functional element level and at the organizational level in the Department and the suborganizational level at posts. Except for the software impairment provision in 4 FAM 735.6, obsolescence is recognized in the useful life established for determining depreciation;

- (2) **Personal property depreciation rates.** Depreciation rates are established on a straight-line basis for the estimated useful life of respective depreciable fixed assets. The owning organization is responsible for determining the useful life of the personal property asset except for aircraft, which is provided for in 4 FAM 736.2-1, paragraph c. The depreciation rate will reflect estimated salvage value, which for personal property is standardized at 10 percent, except where noted in this subchapter (e.g., software, armored vehicles, and property held by contractors in high-risk areas). When property is transferred to the Department from another Federal agency, the useful life used by the transferring agency should be taken into consideration when determining the remaining useful life of the property. Salvage values for such transferred property are recorded at the lesser of:
- (a) The amount designated by the transferring agency; or
 - (b) The amount that would be applicable if the Department had purchased the item;
- (3) **Internal use software.** As a general rule, capitalized software property is amortized over a 3-to-5-year useful life, as designated by the developing entity. While SFFAS No. 10 does not specify a specific amortization time period, Bureau of the Comptroller and Global Financial Services (CGFS) policy limits the amortization period to 5 years or less. However, if the software-owning organization provides a justification for a longer useful life, the managing director of the Financial Policy, Reporting and Analysis Directorate (CGFS/FPRA) will consider an amortization schedule consistent with the software's useful life. Amortization begins the first day of the first full month after the software receives Information Technology Change Control Board (IT CCB) or local Change Control Board (CCB) approval and an authorization to operate from the Department's Designated Approving Authority. Software does not have a salvage value. See 5 FAM 814, 5 FAM 619, and 5 FAM 864, paragraph d.

4 FAM 735 ACCOUNTING FOR INTERNAL USE SOFTWARE

(CT:FIN-433; 09-13-2013)

SFFAS No. 10, Internal Use Software, identifies the accounting requirements for software designed for internal use. Essentially the standard requires software purchased or developed for internal needs to be treated as an asset in the Department's general ledger if it meets the definition and capitalization criteria identified in section 4 FAM 735 and in section 4 FAM 734.2, subparagraph a(4), respectively. The capitalized cost for the software is amortized in accordance with its expected useful life.

4 FAM 735.1 Requirements for Capitalizing Internal Use Software

(CT:FIN-414; 05-05-2011)

- a. Not all software internally developed or contractor-developed software procurements need to be capitalized. To assess the criteria for capitalizing a software development project or procurement action, a plan must be prepared that identifies the following:
 - (1) Functionality of the proposed software investment;
 - (2) Estimated cost for the software portion; and
 - (3) Estimated useful life upon delivery/acceptance of software.
- b. A decision to capitalize internal-use software requires some judgment, exercised in accordance with the guidance in 4 FAM 735. Investments in internal-use software must be capitalized when the investment is projected to meet all three of the following requirements:
 - (1) Create or significantly enhance existing Department functions or capabilities;
 - (2) Meet or exceed the Department-determined cost threshold for the investment (see 4 FAM 734.2, subparagraph a(4), and 14 FAM 425.6-3(B)); and
 - (3) Have an estimated useful life of 2 years or more.
- c. Projects to be capitalized must follow the instructions set forth in the Department's Capital Planning and Investment Control Program Guide and administered by the e-Gov Program Management Office.
- d. Projects that do not create a new function or substantially enhance an existing capability are not capitalized. An example would be a minor software modification resulting from ongoing systems maintenance, which would be considered a modification to an existing function. The cost would not be capitalized even if the anticipated cost exceeds the capitalization threshold and the resulting change would have a useful life of more than 2 years.

4 FAM 735.2 Accounting Guidance Applies to Internal Use Software Only

(CT:FIN-384; 06-19-2007)

Since the Department does not, generally, develop software for external parties or other government entities, the accounting guidance in 4 FAM 730 does not cover software sales or licenses to third parties. Should a circumstance occur whereby Department-developed software is offered for sale or license to an external party,

the accounting for a sale or license should be coordinated with the Office of the Deputy Chief Financial Officer.

4 FAM 735.3 Software Development and Procurement Options

(CT:FIN-394; 08-15-2008)

- a. Software investments generally take one of the following forms:
 - (1) In-house developed. Software developed by Department contractor and/or direct-hire employees. New software code is developed based on a concept design or plan;
 - (2) Commercial off-the-shelf (COTS) procurements;
 - (3) Government off-the-shelf (GOTS) procurements; or
 - (4) Mixed COTS/GOTS procurements and in-house development.(See 5 FAM 900 and 1000 for IT acquisition and planning requirements.)
- b. For both internally developed and off-the-shelf software investments, the costs capitalized must include all the direct costs needed to create, install, configure, and test the software, as well as any cost associated with initial user training, training materials, and user documentation prior to or at the point of final acceptance by Information Technology Change Control Board (IT CCB) or local Change Control Board (CCB) and an authorization to operate from the Department's Designated Approving Authority (see 4 FAM 735.5).
- c. Direct costs would include contractor and Department personnel and initial training costs associated with creating or procuring, implementing, and testing the software. Hardware and software license costs are to be included if costs incurred to perform the work (e.g., special platform that will serve no other purpose) are not captured as an element of personal property (e.g., contractor-furnished equipment that is not purchased under object code 3100).
- d. Indirect costs should also be identified and included in capitalized costs in accordance with 4 FAM 734.1. A project code should be used for all direct costs, and indirect costs should be estimated during the period the software is in development.
- e. Many software development projects require a mixture of software technologies (e.g., COTS/GOTS and in-house development) to achieve a desired functionality or capability. When this occurs, the cost of the project should be capitalized in accordance with 4 FAM 735 when the total estimated cost for the mixed software development effort is projected to exceed the capitalized threshold for software development (see 4 FAM 734.2, subparagraph a(4)).

4 FAM 735.4 Commercial off-the-Shelf/Government

off-the-Shelf (COTS/GOTS) Licenses

(CT:FIN-384; 06-19-2007)

- a. For commercial off-the-shelf/government off-the-shelf (COTS/GOTS) software purchased for a general purpose function, the initial license cost (if applicable) is capitalized as a software development cost, as well as annual license costs that must be incurred as part of a COTS/GOTS configuration and testing process. However, annual license costs after the software has been configured and accepted by Information Technology Change Control Board (IT CCB) or local Change Control Board (CCB) approval are not capitalized and should be expensed in the period incurred.
- b. Costs for follow-on licenses (e.g., corporate licenses for deployment purposes) should be treated in accordance with 4 FAM 734.2, subparagraph a(4), or treated as capital leases if the license agreement is consistent with the leasing criteria under 4 FAM 734.2, paragraph b. Site licenses needed to deploy software at additional locations should be capitalized as personal property if purchased in bulk or expensed if the site license cost does not exceed the capitalization threshold for personal property.

4 FAM 735.5 Capturing Software Costs

(CT:FIN-433; 09-13-2013)

- a. The accumulation of costs to be included in capitalization may begin only after:
 - (1) Management authorizes and commits to a computer software project and believes that it is more likely than not that the project will be completed;
 - (2) The conceptual formulation, design, and testing of possible software project alternatives have been completed; and
 - (3) It is determined that the software will be used to perform the intended function with an estimated service life of 2 years or more.
- b. The accumulation of capitalized software costs will terminate on the date the software is accepted by the Information Technology Change Control Board (IT CCB) or local Change Control Board (CCB) approval is authorized to operate by the Department's Designated Approving Authority. Costs incurred after final acceptance testing has been successfully completed and costs to convert, purge, cleanse, or reconcile data should not be capitalized. In instances where a formal acceptance procedure is not performed by IT CCB or the local CCB and the Department's Designated Approving Authority, the software will be considered accepted as of the date the software is placed in service. Should a circumstance occur whereby software is prematurely placed in service without a formal procedure and additional costs must be incurred to meet an appropriate operating performance, the Bureau of the Comptroller and Global Financial Services, Office of Financial Reporting and Analysis (CGFS/FPRA/FRA) must be consulted on the need to capitalize the additional cost.

4 FAM 735.6 Accounting Treatment for Impaired or Terminated Software Development

(CT:FIN-384; 06-19-2007)

- a. A loss due to software impairment is recognized and measured when one of the following occurs:
 - (1) The software is no longer able to perform the service intended and will be removed from service; or
 - (2) A significant reduction in the capability, function, or use of the software occurs, and it is unlikely the capability or use will be restored.
- b. If impaired software remains in use, the impairment loss should be measured as the difference between the book value and either:
 - (1) The cost to acquire software that would perform similar functions (that is, the remaining unimpaired functions); or
 - (2) The portion of the book value attributed to the remaining functional elements of the software.
- c. A loss is recognized when the software is judged impaired, and the book value of the asset should be reduced accordingly. If a software license or other element of the residual software has a net realizable value (NRV) that can be used in another functional area, the book value should be reduced to the NRV and amortized over any remaining useful life. If a book value of the remaining unimpaired functions cannot be determined at the point of impairment, any remaining book value should be amortized over the remaining useful life of the software or until the planned date to take the software out of service, whichever is shorter.
- d. If management determines that it is no longer likely that software under development will be completed and placed in service, the software-in-development cost up to the termination date will be reduced to the expected NRV, if any. Any difference between the software in development cost and the NRV will be recognized as a loss in the year the software development was terminated.

4 FAM 736 U.S. GOVERNMENT-OWNED PROPERTY HELD BY CONTRACTORS OR HOST GOVERNMENTS

4 FAM 736.1 General Provisions

(CT:FIN-433; 09-13-2013)

- a. Property for which the U.S. Government has title but is in the hands of contractors or host-country governments, such as in the case of bilateral agreements and other foreign assistance, is accounted for as assets of the Department and included in its financial reporting as general property. Much of the Department's contractor-held property is either aviation assets or vehicles. However, contractor-held property can fall into any one of the personal property categories discussed in 4 FAM 733.1-3, paragraph b. Due to the nature of the aviation assets, certain unique provisions apply. These are contained in 4 FAM 736.2-1. There are also special provisions that apply to contractor-held property in high-risk areas, as described in 4 FAM 736.3.
- b. The same capitalization thresholds as apply to other personal property must apply to these assets. Contractor-held property should be reported at the dollar cost to acquire or the dollar value/cost identified when furnished by the Department. Transferred property to the contractor from another Federal agency or non-U.S. Government owner should be reflected at the cost basis of the property transferred. When no cost basis for the property is identified by the transferring entity, the value assigned to the property on the date of transfer should be used. The specific costs to be identified are described in 4 FAM 734. Identify property acquisition or transfer dates with the reported cost information.
- c. Department contractors with U.S. Government-owned property that is acquired by or transferred to custody of the contractor and meets the capitalization thresholds must report property holdings quarterly to the contracting officer's representative (COR) with a copy to the contracting officer and the Bureau of the Comptroller and Global Financial Services (CGFS). Except for the inventory submission in conjunction with the physical inventory described in paragraph d of this section, quarterly dispositions and transfers may be reported in lieu of a complete inventory once a baseline of the contractor-held property is established. The COR is responsible for obtaining the required property data similar to that obtained for Department-held property, including acquisition cost. The COR is also responsible for resolving with the contractor any discrepancies in the quarterly or annual reporting (e.g., unexplained variances).
- d. When appropriate, a contracting officer may designate another individual to perform the function described in paragraph c of this section. All designations must be in writing and be approved by the responsible bureau executive director or equivalent management level.
- e. Contractors are required to perform a physical inventory annually of the U.S. Government-owned property in their custody, consistent with contract terms, and to provide a written assurance by a senior official of the contractor as to the accuracy of the inventory information submitted to the Department. The property information and annual assurance are to be submitted in accordance

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with contract provisions or other instructions issued by the Office of the Procurement Executive (A/OPE) and the contracting office.

4 FAM 736.2 Bureau of International Narcotics and Law Enforcement Affairs (INL) Aviation Assets

4 FAM 736.2-1 Aircraft

(CT:FIN-414; 05-05-2011)

- a. Aircraft property held by Bureau of International Narcotics and Law Enforcement Affairs (INL) contractors is classified as general PP&E. Aircraft (i.e., fixed-wing or rotary aircraft) and aviation program component property is recorded at cost on the purchase/transfer-in date when the title passes or the date placed in service, whichever comes first. The cost basis of the property must be determined by one of three measures, according to the following hierarchy:
 - (1) Acquisition (purchase) cost, if known, plus the cost of refurbishment necessary to allow the unit to be placed in service or used as a spare;
 - (2) Net book value (NBV) on the books of the transferring agency if acquired from another Federal entity, plus the cost of refurbishment necessary to allow the unit to be placed in service or used as a spare; or
 - (3) If no other cost information is available, the manufacturer-suggested book value for a refurbished piece of equipment that is operational and placed in service.
- b. All fixed-wing and rotary aircraft must be capitalized regardless of value, type, and mission configuration.
- c. Capitalized fixed-wing and rotary aircraft will have a useful life of 10 years for INL airwing and 5 years for nonairwing. Depreciation will be computed on a straight-line basis when 4 FAM 736.3 is not applicable. The depreciation rate will be based on a 10 percent salvage value.

4 FAM 736.2-2 Repairs and Improvement to Bureau of International Narcotics and Law Enforcement Affairs (INL) Aircraft

(CT:FIN-433; 09-13-2013)

- a. Repairs to Bureau of International Narcotics and Law Enforcement Affairs (INL) aircraft and program property must be expensed in the year performed when the repairs are routine and overhaul of the entire aircraft or program property is not required. Both the parts and the cost of the repair are expensed when the routine or normal repairs are required to keep the property operational.

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- b. Major/complete overhauls of fixed-wing and rotary aircraft require special accounting treatment when the property requires more than an engine or major component from the spare parts inventory. When an aircraft or other capitalized property is sent to a facility for a complete overhaul, substantial modification, and/or refurbishment, the accounting records will reflect a change to the status of the aircraft, and all depreciation of the property will cease. A disposal will be recorded in accordance with INL information regarding the date the aircraft is taken out of service.
- c. When the aircraft (with same tail number) is subsequently returned and placed in service, all overhaul and/or refurbishment costs to the aircraft, including the cost of shipping to and from the overhaul/maintenance facility, will be recorded as part of the basis for the property. Given the substantial nature of the work performed in the overhaul process, depreciation for the overhauled aircraft will be based on a new useful life and computed in the same manner as a new acquisition of similar property.
- d. In the event of abnormal conditions not addressed by paragraphs b and c of this section, the Office of Accounting Operations (CGFS/F/AOD), in consultation with the Financial Policy, Reporting and Analysis Directorate (CGFS/FPRA), will determine the specific accounting treatment to apply on a case-by-case basis.

4 FAM 736.3 Contractor-Held Property in High-Risk Areas

(CT:FIN-433; 09-13-2013)

- a. For property held by contractors in high-risk areas where the property could be heavily damaged or completely destroyed, the depreciation convention may be accelerated and/or the useful life shortened to no more than 36 months to reflect operating conditions. Property in high-risk areas will have zero salvage value. The Deputy Chief Financial Officer (CGFS/DCFO) or designee is responsible for determining high-risk areas for purposes of this FAM provision and approving the depreciation convention and any other special treatment for property in these areas.
- b. When the CGFS/DCFO determines that conditions in an area warrant a designation as high risk, acquisitions after the date of the determination will be at the accelerated rate, and existing property with more than 24 months of useful life remaining will be fully depreciated by the end of the next full fiscal year. When the CGFS/DCFO determines that conditions in the area are no longer high risk, all existing property will continue to depreciate at the accelerated rate without a salvage value, but new acquisitions will be handled in accordance with the requirements in for other personal property (see 4 FAM 734.3).

4 FAM 737 ACCOUNTING FOR REAL PROPERTY, PLANT, AND EQUIPMENT (PP&E)

(CT:FIN-394; 08-15-2008)

This section pertains to the accounting treatment and responsibilities of organizations dealing with real property owned or leased by the Department. Additional guidance concerning overseas real property management is contained in 15 FAM.

4 FAM 737.1 Real Property Under Statement of Federal Financial Accounting Standards

(CT:FIN-433; 09-13-2013)

- a. Consistent with 4 FAM 731.2, SFFAS No. 6, as amended by subsequent standards—particularly SFFAS No. 29—requires all real property to be designated as either:
 - (1) General;
 - (2) Heritage; or
 - (3) Stewardship land.
- b. SFFAS No. 6 identifies accounting requirements for the costs associated with real property designations. All Department real property designations must be tracked in accordance with the SFFAS No. 6 cost requirements for these designations.
- c. SFFAS No. 6 requires cost capitalization and depreciation accounting. Capitalization is the recording and carrying forward into future periods any expenditure, the benefits or process from which will then be realized. Depreciation accounting is the systematic and rational allocation of the acquisition cost of an asset (e.g., real property), less its estimated salvage or residual value, over its estimated useful life.
- d. The Bureau of the Comptroller and Global Financial Services (CGFS) will incorporate real property designations into the Department's financial fixed asset subsidiary ledgers.
- e. Except for heritage real property and stewardship land, the real property PP&E meeting the direct-cost capitalization thresholds in 4 FAM 738.1 are to be recorded as an asset at cost and include appropriate direct and indirect costs.
- f. All U.S. Government-owned real properties, except for land, and the associated renovations, improvements, or betterments for land and other real property must be depreciated (straight-line method) in accordance with their estimated useful lives.

4 FAM 737.1-1 Real Property (PP&E) Management and Reporting Responsibilities

(CT:FIN-433; 09-13-2013)

- a. The Bureau of Overseas Buildings Operations (OBO) will provide general oversight of all overseas real property, including costs to acquire, construct, improve, and maintain real property. OBO is responsible for project management, establishment of OBO project codes, real property budget/cost controls, and designation of culturally significant assets (i.e., heritage property). OBO is also responsible for notifying the Bureau of the Comptroller and Global Financial Services (CGFS) when real property is acquired, constructed (date of acceptance of substantial completion), sold, or impaired (rendered unusable due to partial destruction, abandonment, etc.), as well as providing deferred maintenance information for reporting in the financial statements.
- b. For purposes of this section, impaired property would be Department-owned property that is not available for U.S. Government use for an indefinite period of time, if ever. Examples of impaired property would be contaminated property that occurs from hostile forces or natural disasters, seriously damaged property from fires or other natural occurrences, and restricted access to U.S.-owned properties by a host government.
- c. The Bureau of Administration (A) is responsible for management of real property owned or controlled by the Department in the United States. The A Bureau Office of Operations (A/OPR) is responsible for project management of U.S. located property acquisitions, renovations, and betterments and for providing real property costs that must be capitalized. The A bureau is also responsible for managing domestic heritage property; capturing deferred maintenance information for domestically held properties; and for submitting required real property information to the Office of the Deputy Chief Financial Officer (CGFS/DCFO) for financial statement reporting.
- d. The individual post management officer has the following primary responsibilities. This effort is supported by the post financial management, facilities management, and general services offices:
 - (1) Recording accurate cost data;
 - (2) Accepting substantial completion data for post-managed construction and renovation projects;
 - (3) Notifying disposal proceeds to CGFS and OBO/RM/FM;
 - (4) Entering data in the OBO real property accountability system; and
 - (5) Working with CGFS and OBO on real property cost information matters.
- e. The Office of Financial Policy (CGFS/FPRA/FP) is responsible for issuing real property accounting policy. As described in this subchapter, CGFS records and

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maintains real property accounting information in the financial system fixed asset subsidiary. Also, CGFS provides quarterly reports on construction-in-progress projects and projects in excess of designated thresholds (see 4 FAM 738.1) with no assigned capital project type for the Bureau of Overseas Buildings Operations (OBO) review. The Office of Financial Reporting and Analysis (CGFS/FPRA/FRA) staff prepares the financial statements and supporting schedules related to real property. The Financial Policy, Reporting and Analysis Directorate (CGFS/FPRA) and OBO will jointly assess indirect charges that will be applied to real property costs.

4 FAM 737.1-2 Project Management for Overseas Real Property

(CT:FIN-433 09-13-2013)

- a. Construction, acquisition, and capital improvements to overseas real property, as well as maintenance projects, are managed by use of project codes to ensure that all costs for the projects are identified and recorded. For OBO-managed projects, the Office of Cost Management (OBO/PDCS/COST) prepares a current working estimate at the time the project is initiated. When the project is not the responsibility of the Cost Management Division, the Office of Facility Management (OBO/CFSM/FAC) develops the current working estimates.
- b. For any construction, acquisition, or improvement project that is estimated to exceed the direct-cost capital thresholds in 4 FAM 738.1, OBO must designate the project code as being a capitalized project in accordance with instructions provided by the Bureau of the Comptroller and Global Financial Services (CGFS). CGFS will ensure that all project codes so designated will be reflected properly in the financial management system general ledger as capitalized costs.
- c. Project codes must be used for all OBO projects. If a single project code is used for a major renovation or restoration involving multiple properties, OBO and CGFS should determine the completion date(s) and cost allocation method, if needed, to ensure that capitalization requirements can be properly identified and recorded by CGFS.
- d. Quarterly, CGFS will provide a report and OBO will review all open OBO projects estimated to meet capitalization requirements. OBO will determine if the project is ongoing, completed, temporarily inactive but continuing, canceled, or indefinitely suspended and inform CGFS as to the project status. CGFS, in coordination with OBO, will make the necessary accounting adjustments to the in-process accounts. If the project is completed, the steps described in 4 FAM 737.4-6 should be followed.
- e. Quarterly, CGFS will provide a report and OBO will identify and review noncapitalized projects whose actual costs exceed the capitalization threshold to determine if these projects should be capitalized. If necessary, OBO will correct the project designation and notify CGFS, who will work with OBO to

make the necessary accounting corrections.

4 FAM 737.2 Classification of Property Accounts

(CT:FIN-433; 09-13-2013)

In addition to the SFFAS No. 6 designations of PP&E designations described in 4 FAM 737.1, general ledger (GL) accounts and balances will be established for the following categories:

- (1) Land (GL account 1711);
- (2) Land Improvements (GL account 1712);
- (3) Construction in Progress (GL account 1720 is the summary account. There are separate accounts for major repairs and renovations, 1721; leasehold improvements, 1722; new construction, 1723; and land improvements, 1724);
- (4) Buildings, including improvements and betterments (GL account 1730);
- (5) Other major facilities or structures, as determined appropriate by the DCFO, OBO, and/or the Office of Facility Management Services (A/OPR/FMS) in the Bureau of Administration (GL account 1740);
- (6) Capital Leases (GL account 1810); and
- (7) Leasehold Improvements (GL account 1820).

4 FAM 737.2-1 Property Records and Systems

(CT:FIN-394; 08-15-2008)

The financial management system must accurately reflect the cost of capitalized real property in various categories and the accumulated depreciation or amortization. Procurement, property-record maintenance, and related accounting operations must be integrated to the maximum extent possible and be cost effective so that entries to the property records and control accounts will be accomplished via a single record or single set of records controlling the acquisition, construction, improvement, or disposition of the real property.

4 FAM 737.2-2 Reconciliation of Accounting Records to Property Records

(CT:FIN-433; 09-13-2013)

The management officer at each post must annually conduct a physical inventory of real property. A/OPR/FMS will conduct a physical inventory of any owned domestic real property at least annually. Inventory procedures and accounting record adjustments must be applied on a consistent basis from one fiscal year to another. The results of the physical observations must be reconciled with the real

property records (e.g., Buildings Management Integrated System (BMIS) for overseas real property). The management officer will assist the Bureau of the Comptroller and Global Financial Services (CGFS), as needed, with any variances between post real property records and the financial fixed asset system.

4 FAM 737.3 Accounting Designations and Cost Treatment for General Real Property, Heritage, and Stewardship Land

(CT:FIN-394; 08-15-2008)

This section covers the accounting designations and cost treatment for real property.

4 FAM 737.3-1 General Real Property Buildings and Structures

(CT:FIN-433; 09-13-2013)

- a. Buildings and other structures used to support U.S. Government foreign affairs programs that are useable by other governmental or nongovernmental entities (e.g., private companies, foreign governments, or individuals) are classified as general property. In 1997, the Department identified and valued all general real property from available property records. The Department determined the estimated present value of the properties and then discounted them to their estimated historical costs. The resulting valuation became the real property asset value as of September 30, 1996 for general ledger purposes.
- b. Properties acquired after September 30, 1996 are recorded and based on the historical cost to acquire or construct the real property buildings and structures. Building/structure costs must be separately identified from the costs of the associated land. In instances where an acquisition includes land, building(s), or other structure(s), the acquiring organization (e.g., OBO or A/OPR) must determine an appropriate cost allocation for the land, as well as each building or structure.
- c. When acquisitions involve buildings when no land conveys, or there is no basis for determining the land value, there will be no separate assignment of cost to the land. Situations where separate land costs are not recorded include land with host-country restrictions on land ownership, long-term leased land at no or nominal amounts, and condominium properties in multi-unit property where a land cost is not identified or cannot readily be determined.
- d. Land rental costs must be expensed in the current period, even if there is an owned or newly constructed building on the land. However, the Bureau of the Comptroller and Global Financial Services (CGFS) will record betterments to land under such agreements as capital improvements, consistent with 4 FAM 737.4-5.

4 FAM 737.3-2 General Real Property Land

(CT:FIN-394; 08-15-2008)

- a. Except as noted in 4 FAM 737.3-1 c, land costs must be identified separately from the costs associated with the general buildings or structures built on this land. Costs associated with land engineering and development may be recorded as part of the building when such costs cannot be easily separated from other building costs.
- b. Land is not a depreciable asset. However, improvements to land will be capitalized and depreciated over the expected useful lives of the improvements (see 4 FAM 737.4-5 and 4 FAM 738.1 (2) for the definition and accounting treatment for improvements and repairs to general land).

4 FAM 737.3-3 Heritage Real Property

(CT:FIN-414; 05-05-2011)

- a. Heritage real property consists of buildings or structures that have historical, architectural, cultural, or natural significance to the host country, or have been utilized as locations for conducting significant diplomatic activity (e.g., treaty negotiations and treaty-signing ceremonies).
- b. OBO is the organization responsible for establishing criteria and designating heritage real property in overseas locations (also referred to as culturally significant property). The Bureau of Administration, in conjunction with the General Services Administration, will designate Department of State-owned heritage real property within the United States.
- c. Heritage properties may be utilized well beyond their intended useful life and may be preserved indefinitely, even if the cost of maintenance is extensive.

4 FAM 737.3-4 Multi-use Real Property Heritage Assets

(CT:FIN-433; 09-13-2013)

- a. Heritage property may have a multi-use function, meaning it is a heritage asset used as a general asset. For example, a heritage asset may be used as a chief of mission (COM) residence instead of another residential property with a general PP&E designation.
- b. CGFS will designate multi-use heritage assets as heritage assets based on information provided by OBO. However, the accounting for multi-use heritage assets may mirror requirements for general real property (see 4 FAM 737.3-5 b).

4 FAM 737.3-5 Accounting for Heritage Assets

(CT:FIN-394; 08-15-2008)

- a. Heritage assets, unless they are multi-use heritage assets, will be recorded in the financial records as follows:
 - (1) The acquisition cost of a heritage asset must be recognized as an expense in the period incurred and will not be capitalized;
 - (2) The cost of improving, reconstructing, or renovating a heritage asset must be recognized as an expense in the period incurred and will not be capitalized;
 - (3) No costs will be recognized in the accounting system or for financial reporting purposes when heritage assets are transferred from other Federal entities; and
 - (4) The cost of heritage assets acquired through donation or devise must not be recognized in the accounting system or for financial reporting purposes.
- b. If the heritage asset is a multi-use heritage asset (i.e., it is an asset used to support general-purpose functions) and the cost incurred is an improvement, acquisition, donation, or transfer of heritage property, the costs will be capitalized in accordance with the accounting procedures for general property.

4 FAM 737.3-6 Stewardship Land

(CT:FIN-414; 05-05-2011)

- a. This category of assets is only for undeveloped land holdings. Stewardship land is land not acquired for, or in connection with, other general PP&E. If the land is acquired for, or in connection with, an item of general PP&E (e.g., employee overseas housing, additional office annexes, etc.) it should be categorized as general PP&E. The acquisition cost of stewardship land should be recorded in the period the cost is incurred.
- b. The Department of State does not hold stewardship land. It is unlikely that the Department will ever be required to hold this particular type of asset. In the event stewardship land is acquired, donated, or otherwise conveyed, the land will not be valued for financial reporting purposes, and no costs will be assigned to the land. Any cost that may arise from acquiring the stewardship land will be expensed in the year incurred. The official property records will reflect the number of land parcels owned and estimated square miles for each parcel.

4 FAM 737.4 Accounting for Real Property Investments, Dispositions, and Conveyances

(CT:FIN-433; 09-13-2013)

- a. **Acquisitions, construction, and betterments of property.** The investment

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costs to be recorded for real property transactions are described in 4 FAM 737.4-1 through 4 FAM 737.4-6.

- b. **Disposition of property.** The Bureau of the Comptroller and Global Financial Services (CGFS) will adjust real property subsidiary records for acquisition cost and depreciation values of retirements, losses, or other means of property disposal, including property destroyed or demolished. Prior to the disposal of real property, all property must be inspected by management officials (e.g., GSO, RSO, etc.) for any classified material and a Form DS-586, Turn-in Property Inspection Certification, prepared and affixed to each appropriate item having drawers (e.g., built-in desks or file cabinets or any data from computer equipment, etc.).
- c. Disposition of leasehold improvements. CGFS will adjust leasehold improvement subsidiary records for destroyed or damaged improvements. Similarly, if the leased property is terminated, all remaining costs for existing leasehold improvements will be written off. Losses will be recognized for the costs that were not fully depreciated at the time leasehold improvement adjustments or write-offs are recorded.
- d. Retired property must be separately classified in the financial management subsidiary accounts. Gains and losses on disposal of assets will be recognized separately in the accounts.
- e. Real property exchanges with a non-Federal agency must be recorded at:
 - (1) The fair value of the property that is exchanged or acquired at the time of exchange. The value selected must be based on a decision as to which value is more readily determinable at the time of the exchange; or
 - (2) The cost recorded for the property surrendered net of any accumulated depreciation when the fair values in paragraph (1) are not readily determinable.

Gains or losses realized on real property exchanges will be recorded in separate accounts, and the amount of gain or loss will be the difference between the value selected and the recorded investment in the property exchanged.
- f. Reimbursable transfers from another Federal agency must be accounted for on the basis of the transfer price, as determined by agreement or application of appropriate statutory requirements or regulations, but at not less than its estimated useful value.
- g. **Transfers from other Federal entities.** The cost of the property transferred without reimbursement from other Federal agencies must be the cost recorded by the transferring entity less the accumulated depreciation or amortization. If these amounts cannot be determined, the cost of the property must be its fair value at the time transferred.
- h. **Donations, devise, or judicial process.** The cost of general real property buildings, land, or improvements acquired through donations, devise (bequest),

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or judicial process must be the fair value of the property at the time acquired by the Department. However, heritage property will be recorded at zero regardless of any residual net book value (NBV) if the acquired property will not have a mixed-use heritage designation.

- i. **Forfeiture.** The cost of real property acquired through forfeiture must be determined in accordance with the specific property accounting treatment described in the Statement of Federal Financial Accounting Standards (SFFAS) No. 3.

4 FAM 737.4-1 Acquisition Cost for Purchasing Real Property

(CT:FIN-394; 08-15-2008)

- a. To the extent a cost can be associated with a particular real property procurement, general real property acquisition costs must be accumulated and capitalized in accordance with the capitalization thresholds identified in 4 FAM 738.1 (1). Costs associated with a purchase include:
 - (1) Title searches, legal fees, and other real estate transfer or settlement costs for the purchase;
 - (2) Engineering, architectural, and other non-Department services for structural integrity or defect determinations;
 - (3) Easements or right-of-way costs that may be incidental to the purchase decision; and
 - (4) Initial fix-up or make-ready costs to meet Department of State office or residential occupancy standards (e.g., safe haven locations, fire suppression/safety fixtures, and reinforced flooring).
- b. The Bureau of Overseas Buildings Operations (OBO) will establish a project code and property number in the Buildings Management Integrated System (BMIS) for each acquisition. Post financial management officers must record the costs of real property acquisitions in the financial management system referencing the project code established for the purchase.

4 FAM 737.4-2 Accounting for Land Purchase Options

(CT:FIN-394; 08-15-2008)

- a. The acquisition cost of land includes any land purchase options. A land purchase option is the cost of an option that was paid to purchase the land at some future date. All land purchase options should be associated with a specific land parcel.
- b. When a parcel of land is purchased, any existing option cost for the land purchase will be capitalized as part of the land acquisition cost. Any land purchase options for sites not purchased will be expensed.

4 FAM 737.4-3 Accounting for Real Property Acquired for Security or Set-back Purposes

(CT:FIN-433; 09-13-2013)

- a. Real property buildings and structures acquired after fiscal year 2008 for security set-back reasons are recorded at cost and are not depreciated. The land/building cost allocation must be performed as noted in 737.3-1b. To qualify for this accounting treatment, the buildings and structures must be identified in accordance with all of the following:
 - (1) Acquisition is solely for security reasons;
 - (2) The buildings and structures are vacant or unused; and
 - (3) Maintenance will be minimal, and resale or lease to safe tenants is restricted by written determinations issued by OBO, Bureau of Diplomatic Security, or the post.
- b. In the event that the use of the property is changed to active operation, OBO must notify CGFS immediately to allow the building depreciation to be started.

4 FAM 737.4-4 Costs for Construction, Renovation, and Capital Improvements of Department-Owned Real Property

(CT:FIN-394; 08-15-2008)

- a. The posts and OBO must record costs for constructing or improving real property using a project code established by OBO (see 4 FAM 737.1-2). The project code tables in the financial management system will be configured so that the costs are either capitalized or expensed in accordance with the building or structure designation (e.g., general purpose, heritage, or mixed-use heritage) and capitalization thresholds. Costs that are to be capitalized upon completion will be accumulated in a construction-in-progress account.
- b. Capital improvements for general real property must extend the useful life of the building or structure. Costs that are capitalized as part of the construction, renovation, and improvements include:
 - (1) Engineering, architectural, and other non-Department services for designs, plans, specifications, and surveys;
 - (2) Construction contracts for labor, materials, and other construction needs;
 - (3) Easement and right-of-way costs for buildings and other structures;
 - (4) Costs for cleared American guards, construction security technicians, and securing the construction area;
 - (5) Demolition costs for existing structures;
 - (6) Applicable direct costs (Department employees and personal service contractors), Government-furnished materials, supplies, and other direct

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charges;

- (7) Applicable share of Department-owned equipment (e.g., cranes, heavy equipment, etc.) and facility costs used in the construction work;
 - (8) Applicable indirect overhead costs as defined in 4 FAM 738.2;
 - (9) Fixed and severable equipment that are not likely to be removed if the building/structure is sold, such as HVAC/generators, elevators and escalators, and their installation cost;
 - (10) Inspection, supervision, and administration of construction contracts and construction work;
 - (11) Legal fees and damage claims; and
 - (12) Fair value of contributed facilities, utilities, labor, materials, supplies, equipment, etc.
- c. Capital improvements would include but would not be limited to additions to the building, rehabilitation, replacement of heating/air-conditioning systems, power/wiring upgrades, sewer-treatment/waste-water processing upgrades, asbestos removal, and interior renovations to accommodate special program requirements or configurations.
- d. If a project that has been classified as capitalized is cancelled, or the scope is reduced such that it no longer meets the criteria for a capitalized asset, the costs that have been recorded as construction-in-process will be recognized as an expense in the period in which the cancellation or change in scope is reported.

4 FAM 737.4-5 Capital Improvements for Land Associated with General Purpose Property

(CT:FIN-414; 05-05-2011)

- a. Capital land improvements or betterments include roads, driveways, drainage retaining walls, security walls and gates, and improvements that are not directly attributable to a building on the land (land betterments do not include power control units or generators that are directly attached to a building or multiple buildings).
- b. Land betterments should be capitalized if they exceed Department-established thresholds (see 4 FAM 738.1 (2)) and extend the functionality of vacant land and/or access to the buildings and structures on the land. The costs of the improvement must be accumulated in a construction-in-progress project account in the same manner as costs are accumulated for projects associated with buildings.
- c. When constructing a compound of multiple buildings on a single-land parcel, the land betterments may be capitalized as a cost to the entire compound if the costs for individual buildings and structures on the compound cannot be

separately identified.

4 FAM 737.4-6 Project Completions and Lagging Costs

(CT:FIN-433; 09-13-2013)

- a. For a construction project, the project completion date must be the date that the U.S. Government (OBO and/or post) accepts the project as substantially complete (i.e., "substantial completion date") in accordance with the contract provisions. For most projects, this will be evidenced by a formal letter submitted by the U.S. Government back to the contractor. When the construction work is not centrally monitored by OBO, the post management officer (MO) must notify OBO within 30 days after the completion date by submitting the post acceptance of substantial completion letter or by cable. OBO will notify CGFS each quarter of all completions during that proceeding quarter or more frequently if requested by CGFS.
- b. For purposes of computing depreciation, the acceptance of substantial completion date will be the in-service date. Depreciation will be computed in accordance with 4 FAM 738.3.
- c. Real property acquired by purchase must be recorded as an asset of the Department of State as of the "settlement/closing date" under local law. Because of the potential for long lead times for transferring title in many foreign locations, this date will be used as the "constructive ownership" date for purchased property. All purchase contracts must include the date of closing to provide supporting documentation for recording the asset acquisition.
- d. CGFS will record real property acquisitions based on acquisition information provided by OBO and accounting system cost data. Post MO will provide acquisition information to OBO within 30 days after property is acquired consistent with paragraph c. OBO must notify CGFS of acquisitions no less than quarterly (at the end of the quarter) and provide CGFS a copy of the original purchase contract documents, plus an English translation if the contract is written in a foreign language. For purposes of computing depreciation, the in-service date for purchases will be the "constructive ownership" date described in paragraph 4 FAM 737.4-6 c. Depreciation will be computed in accordance with 4 FAM 738.3.
- e. When OBO purchases an unusable or noninhabitable building, and a major renovation or other impediment to occupancy of the property is projected to exceed a 12 month period, OBO must advise the Office of Financial Reporting and Analysis (CGFS/FPRA/FRA) of the projected occupancy date and request an in-service date that is based on the vacancy period. Depreciation on these purchases will begin after OBO advises the Bureau of the Comptroller and Global Financial Services (CGFS) that the property has been put in service, usually when OBO has established the beneficial occupancy date. Depreciation will be computed in accordance with 4 FAM 738.3.

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- f. Lagging costs for real property construction and acquisition may occur after properties are recorded and placed in service. Lagging costs are defined as charges (e.g., invoices) that are received after substantial completion has been issued on the construction project. The charges may result from approved follow-on charges, holdbacks, or other invoice costs that were not submitted prior to the time of completion. Lagging costs should be added to the basis of the property in accordance with paragraphs g and h.
- g. Except for circumstances identified in paragraph h, the time period for recording lagging construction costs must not exceed 24 months from the completion and placing the property in-service. CGFS will monitor any lagging costs for completed projects and record all amounts when the total of these costs exceeds the lagging cost threshold of \$25,000. Amounts for completed projects at the end of the 24-month period that are less than the threshold of \$25,000 will be expensed. Construction or acquisition costs will be recorded after the 24-month period only when they are associated with a separate capitalized betterment meeting capitalization threshold requirements. This provision for lagging costs is effective as of October 1, 2008.
- h. When there are legal proceedings and contract disputes for a completed building or improvement, resulting termination or settlement costs may be added to the cost basis of the property. The 24-month limitation for lagging costs does not apply in these cases.
- i. The Office of the Deputy Chief Financial Officer (CGFS/DCFO) will analyze and set lagging-cost criteria in accordance with historical cost information. Lagging-cost thresholds will be reviewed and revised every 5 years based on historical trends, inflation, and other factors that affect the materiality of recording such costs.

4 FAM 737.4-7 Capital Improvements for Stewardship Land

(CT:FIN-394; 08-15-2008)

Capital improvements for stewardship land (e.g., roads, bridges, drainage ditches, etc.) are not capitalized and should be expensed in the accounting period in which the cost is incurred.

4 FAM 737.4-8 Real Property Capital Projects Funded by Other Agencies

(CT:FIN-433; 09-13-2013)

As described in 15 FAM, OBO is authorized to construct and improve real property in foreign locations for the use by diplomatic and consular operations of the United States, including providing for space for other agencies under the authority of the chief of mission. As such, OBO may receive funding through various funding mechanisms from other agencies. When another agency provides funding to the

Department for OBO to execute a facility project, OBO and CGFS will coordinate on the appropriate accounting treatment for the funding from that agency.

4 FAM 737.5 Accounting for Real Property Leases

4 FAM 737.5-1 Capital Leases

(CT:FIN-394; 08-15-2008)

For accounting and financial reporting purposes, real property leases that meet the criteria of 4 FAM 738.1 (3) must be recorded in Department financial management systems as capital leases and amortized in accordance with 4 FAM 738.3 (3). The cost of property under a capital lease must be equal to the amount recognized as a liability for the lease at its inception (i.e., the net present value of the future minimum lease payments or the fair market value, whichever is less).

4 FAM 737.5-2 Accounting for Operating Real Property Leases

(CT:FIN-394; 08-15-2008)

Operating real property leases are all other leases for buildings, structures, and land that do not meet the capitalized lease criteria. Rental payments for these leases are operating expenses and must be charged to expenses according to the lease payment terms. Minor improvements or repairs to operating leases should be expensed in the current year as well. Major improvements or repairs at Government expense may occur with operating leases given the terms and conditions associated with these leases. If a major improvement is done, the improvement will be accounted for in the same manner as other capitalized leasehold improvements (see 4 FAM 737.5-3).

4 FAM 737.5-3 Capitalized Leasehold Improvements to Leased Real Property

(CT:FIN-414; 05-05-2011)

Leasehold improvements to real property leases must be capitalized if the anticipated cost equals or exceeds the Department-established thresholds (see 4 FAM 738.1 (3)), and the capital improvement extends the useful life of the building or structure. The cumulative costs must be accumulated in a construction-in-process account similar to the manner in which costs are capitalized for construction while the project is underway. Capital improvements would include, for example, the cost of acquiring and installing new ceilings, permanent walls, lighting, air-conditioning, safety and protective devices with a useful life longer than 1 year, and additions and betterments to buildings and other facilities. Leasehold improvements must be capitalized and amortized over a 10-year useful life. Amortization conventions for leasehold improvements are identified at 4 FAM 738.3 (3).

4 FAM 737.6 Repairs, Maintenance, and Minor Improvements

4 FAM 737.6-1 Buildings and Structures

(CT:FIN-394; 08-15-2008)

By definition, repair and maintenance to buildings and structures that do not extend useful life are not capitalized even if the total cost exceeds the dollar threshold. Roof repairs that are not capital improvements; generators that are not classified as capitalized personal property; and underground storage tank replacements are examples of the type of maintenance costs that are expensed. Similarly, minor improvements that are less than the capitalization criteria stated in 4 FAM 738.1 (2) are expensed.

4 FAM 737.6-2 Land

(CT:FIN-394; 08-15-2008)

Repairs, maintenance, and minor improvements to land are normally expensed in the current accounting period and are not capitalized unless the repairs improve or extend the functionality of the land or structure (e.g., sidewalk) located on the land. If the repairs are conducted as part of a new embassy construction (NEC) project, and the costs cannot be easily separated, they may be captured as part of the total NEC project.

4 FAM 738 CAPITALIZING, DEPRECIATING, AND AMORTIZING REAL PROPERTY COSTS

(CT:FIN-394; 08-15-2008)

This section provides guidance on real property capitalization requirements for constructed, purchased, improved, and leased real property. Guidance is also provided for the indirect costs that must be capitalized with the direct costs, as well as the depreciation or amortization convention that must be applied to capitalized amounts.

4 FAM 738.1 Capitalization Criteria for Real Property

(CT:FIN-414; 05-05-2011)

- a. Direct costs will be used to determine if a project meets the capitalization threshold. The following direct-cost capitalization thresholds must be applied to property, plant, and equipment (PP&E) in accordance with the process used to acquire the property:

- (1) **Acquired and constructed buildings and land.** Except for heritage

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assets and stewardship land, all buildings and land acquired by the Department or buildings constructed and owned by the Department must be capitalized regardless of cost;

- (2) **Improvements to land and buildings.** The capitalization threshold for improvements to Department real property is direct cost of \$1 million. This same threshold also applies to real property leasehold improvements;
- (3) **Capitalized real property leases.** The capitalization threshold for the Department's capitalized real property leases is \$1 million. In addition to the threshold, there are other criteria that must be met for capital leases. Leases meeting one or more of the following criteria must be classified as capital leases:
 - (a) Lease transfers ownership to the Government at the end of the lease term (i.e., fixed noncancelable term);
 - (b) Lease contains a bargain purchase option to ensure purchase of the property;
 - (c) Lease term is equal to 75 percent or more of the economic life of the leased property; and
 - (d) Present value at the beginning of the lease for the minimum lease payment is 90 percent or more of the fair value of the leased property.

- b. Capital leases must be recorded as an asset and a liability at an amount equal to the present value at the beginning of the lease for the minimum lease payments during the lease term, excluding any executory costs to be paid by the lessor (e.g., taxes, insurance, etc.). However, if the amount so determined exceeds the fair value of the property, record the fair value. Purchases made under lease/purchase contracts that are in fact purchases (the decision to purchase having already been made) will be treated for capitalization purposes as installment purchases.

4 FAM 738.2 Accounting for Indirect Costs

(CT:FIN-433; 09-13-2013)

- a. In addition to capturing the direct costs for real property construction, improvements, and renovations, the responsible organization must work with the Office of Financial Reporting and Analysis (CGFS/FPRA/FRA) to identify and capitalize the indirect overhead costs associated with Department real property. Indirect costs will be added to direct costs for construction and improvement projects.
- b. Indirect overhead costs for Department real property must include the following components:
 - (1) Oversight organization salary and benefit costs and/or contractor costs for:
 - (a) Supervisory personnel overseeing staff responsible for multiple

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construction/renovation projects or the coding/configuration of software projects;

- (b) Personnel retained as experts in areas related to specialized real property design requirements (e.g., heating/cooling plants, wiring, security, fire suppression, safety, etc.) or software design tools;
 - (c) Supervisory personnel responsible for physical and/or construction security;
 - (d) Personnel supporting the construction or renovation of real property projects or software development/acquisition; and
 - (e) Office space for direct-hire personnel and/or Government-furnished space and equipment for contractor personnel;
- (2) Travel and fixed facility (e.g., office space, utilities, supplies, computer hardware, etc.) costs for organization supervisory and other personnel (e.g., legal, procurement, financial, administrative, etc.) responsible for supporting construction/renovation projects and software development; and
- (3) Fees, licenses, and/or other costs for legal, engineering, construction, or other services that support organization construction, renovation, or software development activities but are not directly attributed to specific projects.
- c. The Financial Policy, Reporting and Analysis Directorate (CGFS/FPRA), in consultation with OBO, is responsible for determining the indirect cost elements or function codes for real property. Either a percentage of direct costs based on historical experience or other methods may be used to allocate the indirect costs. The Deputy Chief Financial Officer (CGFS/DCFO) is responsible for determining the accounting method to use.

4 FAM 738.3 Depreciation and Amortization for Real Property

(CT:FIN-433; 09-13-2013)

Depreciation conventions will be applied to the total costs for general assets that have been constructed, purchased, or exchanged. Amortization conventions will be applied to real property capital leases. Depreciation and amortization will commence on the in-service date:

- (1) **Basic principles.** In accordance with SFFAS No. 6, the accounting system will recognize and record depreciation and amortization on all capitalized general-purpose and mixed-use property based on the useful life of the asset. Depreciation and amortization charges must be recorded by property, budget fiscal year, and fund;
- (2) **Real property.** Depreciation for real property will be computed on a

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straight-line basis and will begin on the date the real property-owning organization reports the asset as completed/placed in service. A 30-year life will be used for most buildings and land improvements recorded after October 1, 2008. Improvements consistent with 4 FAM 737.4 that extend the useful life of an existing building will be depreciated over a 10-year useful life; and

(3) Capital leases and leasehold improvements for real property.

Capital leases will be amortized over the useful life of the asset if capitalized under the criteria identified at 4 FAM 738.1, subparagraphs (3)(a) or (3)(b) and amortized over the period of the lease if capitalized under the criteria identified at 4 FAM 738.1, subparagraphs (3)(c) or (3)(d). Newly leased buildings or other structures will not be amortized until occupied and/or placed into service. Leasehold improvements as defined at 4 FAM 737.5-3 will be amortized over a 10-year useful life.

4 FAM 738.4 Disclosure of Heritage Assets and Stewardship Land

(CT:FIN-394; 08-15-2008)

Since heritage assets and stewardship land are not capitalized, there is no cost or depreciation in the financial management system associated with these property holdings. Heritage assets and stewardship land are disclosed in notes to the financial statements. Disclosure is presented in aggregate totals and includes a description, count of acquisitions and withdrawals, condition, number of items, and status of deferred maintenance. Stewardship land, if any, is disclosed in number of parcels held and estimated square miles. Mixed-use heritage assets are disclosed with other heritage assets, even though they are also accounted for as general-use property (see 4 FAM 737.3-4).

4 FAM 739 DEFERRED MAINTENANCE

4 FAM 739.1 Application and Definition of Deferred Maintenance

(CT:FIN-433; 09-13-2013)

- a. The deferred maintenance policy applies to all Department organizations that own or maintain property and is applicable to all capitalized real and personal property.
- b. SFFAS No. 6 defines and distinguishes "maintenance" from "deferred maintenance" as follows:
 - (1) Maintenance is the act of keeping fixed assets in useable condition. It includes preventative maintenance, normal repairs, replacement of parts

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and structural components, and other activities needed to preserve the asset so that it continues to provide acceptable services and achieves its expected life. Maintenance excludes the activities aimed at expanding the capacity of an asset or otherwise upgrading it to serve needs different from or significantly greater than those originally intended.

- (2) Deferred maintenance is maintenance that is not performed when required or scheduled and as a result is delayed for a future period. Deferred maintenance is a foregone cost that will be recognized in a future period when the Department uses financial resources (e.g., appropriations, user fees, reimbursements, etc.) to perform the maintenance that is currently being deferred.

4 FAM 739.2 Deferred Maintenance Methodologies

(CT:FIN-433; 09-13-2013)

- a. Department organizations may use the following methods to determine deferred maintenance:
 - (1) Life cycle (scheduled maintenance);
 - (2) Condition assessment; and
 - (3) Alternate modeling approaches.
- b. The methods may be applied individually or in combination, provided there is reasonable assurance that an accurate deferred maintenance estimate is developed and reportable.
- c. Selection of the method that is appropriate for an individual Department organization per 4 FAM 737.1-1 will be a business decision of the responsible organization, since the selected method must be compatible with organizational needs and systems. However, in selecting the method to use, each Department organization must recognize that its systems will be subject to audit, and any deferred maintenance information submitted to CGFS/DCFO must meet the reporting requirements for preparing annual financial statements.

4 FAM 739.2-1 Life-Cycle Method

(CT:FIN-394; 08-15-2008)

Life-cycle costing is an acquisition or procurement technique that considers operating, maintenance, and other costs in addition to the acquisition cost of assets. The difference between the anticipated amount of maintenance (e.g., cost to be incurred in the accounting period) and the actual cost of maintenance performed would be deferred maintenance.

4 FAM 739.2-2 Condition Assessment Method

(CT:FIN-394; 08-15-2008)

- a. Condition assessment surveys are periodic inspections of PP&E to determine their current condition and estimated cost to correct any deficiencies. If condition assessment surveys are determined to be the best method of measuring deferred maintenance, the assessments must be prepared by each major class of property, plant, or equipment (see 4 FAM 739.4).
- b. For the property being measured, there must be specific criteria describing the requirements or standards for acceptable operating condition, and this criteria must reflect any changes in the condition requirements or standards that occur in the accounting period being measured (e.g., fiscal year). In addition, condition assessments must provide information on overall condition of the major asset class and an estimate or range of the dollar amounts needed to return the asset class to its acceptable operating condition. For real property, the dollar estimate or range for condition assessments must be on a property-by-property basis.

4 FAM 739.2-3 Alternate Modeling Approaches

(CT:FIN-394; 08-15-2008)

Department organizations may use alternate cost-effective modeling approaches that provide accurate and auditable results towards substantiating deferred maintenance needs and costs.

4 FAM 739.2-4 Combined Methods

(CT:FIN-394; 08-15-2008)

Department organizations may use both a life-cycle and a condition assessment method in a combined process to report deferred maintenance, provided there is a single dollar estimate of the deferred maintenance and the methods used to determine this amount meet the minimum requirements for life-cycle and condition assessment methods identified in 4 FAM 739.2-1, 4 FAM 739.2-2, and 4 FAM 739.2-3. For example, if a piece of real property has a major system within the property (e.g., heating/air-conditioning unit, etc.) that is best managed with a life-cycle method, but the property must have a condition assessment to determine deferred maintenance on other elements of the property (e.g., roof, flooring, painting, etc.), the responsible Department organization may elect to report a combined dollar amount for the property.

4 FAM 739.3 Impaired Assets

(CT:FIN-433; 09-13-2013)

- a. By its status, an impaired asset is often viewed as an asset that is foregoing

maintenance, because of Department inability to conduct the maintenance. However, this view and the cost of an impaired asset should not be confused with the costs associated with deferred maintenance. Unlike deferred maintenance, an impaired asset requires the Department to recognize a cost for the current period. Essentially, an impaired asset net book value (NBV) is reduced to an amount that reflects its condition in the year of asset impairment.

- b. When an organization has a capitalized asset that it considers impaired, it should contact the Office of the Deputy Chief Financial Officer (CGFS/DCFO). Impaired assets that are considered sufficiently material to warrant the recognition of a loss in the general ledger accounts of the Department will be reviewed on a case-by-case basis. Issues that will be considered include current condition, condition at point of impairment, net book value prior to impairment, and Department ability to place the impaired asset back in service in a reasonable time period. Also, consideration should be given to whether future access to the asset would be so impaired that maintenance would be indefinitely postponed and sufficiently material to be a continuing loss instead of deferred maintenance.
- c. Assets classified as impaired should be designated as an impaired asset in the property management system. In the third quarter of each fiscal year, the status of the impaired assets and their condition should be assessed by the owning organization.

4 FAM 739.4 Requirements and Reporting Responsibilities for Deferred Maintenance and Impaired Assets

(CT:FIN-433; 09-13-2013)

- a. The executive director or an equivalent senior management official in the owning organization must submit deferred maintenance information to CGFS/FPRA in accordance with annual CGFS/DCFO reporting instructions and submission dates. In OBO, the managing director for Operations and Maintenance will be responsible for tracking and reporting deferred maintenance. At a minimum, submitted information must contain the following for all property categories managed in the Department (e.g., general purpose, heritage, etc.). In addition, each organization must:
 - (1) Identify the major class of property being reported (e.g., buildings and structures, land, furniture and fixtures, equipment, vehicles, etc.); and
 - (2) State the method(s) of measuring deferred maintenance for each major class.
- b. If a total life-cycle cost process is used to identify deferred maintenance, the information provided must include:

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- (1) The date of the most recent maintenance forecast;
 - (2) The date of the original forecast and an explanation of why changes had to be made;
 - (3) The cumulative amount of deferred maintenance submitted in the prior year;
 - (4) The dollar amount of maintenance for the reporting period that must be added or subtracted from the prior-year cumulative dollar amount;
 - (5) The dollar amount of maintenance actually performed during the period;
 - (6) The difference between the forecast and actual maintenance;
 - (7) Any adjustments to the scheduled amounts that were deemed necessary; and
 - (8) The ending cumulative balance for each major class of asset-experiencing deferred maintenance (e.g., buildings and structures, land, furniture and fixtures, equipment, vehicles, etc.).
- c. For condition assessment or combined methodology, the submitted information must include:
- (1) A general description of the organization's requirement or standard used to assess the operating condition of the asset (e.g., buildings and structures, land, furniture and fixtures, equipment, vehicles, etc.);
 - (2) A summary of any changes made to the requirement or standard during the fiscal year;
 - (3) An annual organizational assessment of asset condition (e.g., excellent, good, fair, poor); and
 - (4) A range estimate of the dollar amount of maintenance needed to return the asset class to an acceptable operating condition consistent with the most current requirement or standard.